

9. ALTERATION IN SHARE CAPITAL

ANALYSIS OF PREVIOUS EXAMINATIONS FOR THEORY QUESTIONS

No.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M19 (O)	M19 (N)	N19 (O)	N19 (N)	N-20(O)	N-20(N)
5.	4	.	.	.	.	.	.	.	.	.	.
6	5
7	.	.	5	.	.	.	.	.	.	.	.	.	.	.	.	.	.
8	3	.
9.	4	.	.	.	3	.	.	.	.	.	.	.	.
12.	4	.	.	.	.	.	.	.	.	.	.	.	.	.	.	.	.
16	5	.	.	.	.

ANALYSIS OF PREVIOUS EXAMINATIONS FOR PRACTICAL QUESTIONS

No.	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M19 (O)	M19 (N)	N19 (O)	N19 (N)	N-20(O)	N-20(N)
1.	5	.	.	.	.	.	.	.	.	.	.	.
7	5	.	.
8.	4	.	.	.	.	.	.	.	.	.	.
9.	.	.	5	.	.	.	.	.	.	.	.	.	.	.	.	.	.
10	4	.	.	.	.	.	.	.	5	.	.
11	6	6	.	.	.

CHAPTER OVERVIEW

SECTION	TOPIC	STARTING PAGE NO.
1.	THEORY FOR CLASSROOM DISCUSSION	9.2
2.	QUESTIONS FOR ACADEMIC INTEREST FOR STUDENTS SELF STUDY	9.15
3.	PRACTICAL QUESTIONS FOR CLASSROOM DISCUSSION	9.17
4.	PRACTICAL QUESTIONS FOR STUDENTS SELF PRACTICE	9.23
5.	SECTION NUMBERS	9.25

SECTION 1: THEORY FOR CLASSROOM DISCUSSION

Q.No.1. Explain the concept of Alteration of “Capital Clause”.

(B) (NEW SM, OLD SM, OLD PM)

ALTERATION OF CAPITAL [Sec 61(1) read with Sec 13 of the Companies Act, 2013]:

- 1) Power to alter Share capital is available only to a limited company having share capital.
- 2) Alteration of Share capital can be done only if authorized by Articles of Association.
- 3) Alteration of Share capital is to be done by alteration of MOA in the General Meeting
- 4) Ordinary Resolution is sufficient for such alteration

MANNER OF ALTERATION:

- 1) Increase authorized share capital¹ by such amount as thinks necessary.
- 2) Consolidate² and divide all or any of its share capital of a larger amount than its existing shares.
- 3) Convert all or any of its fully paid up shares into stock³, and reconvert that stock into fully paid shares of any denomination.
- 4) Sub-divide⁴ the whole or any part of its shares into shares of smaller amount than is fixed by the MOA.

In case of sub-division, the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same.

- 5) Cancel⁵ those shares which have not been taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled.

NOTE:

- 1) However, consolidation and division which results in changes in the voting percentage of shareholders shall take effect only if it is approved by the tribunal.
- 2) The cancellation of shares shall not be deemed to be a reduction of share capital.

NOTICE TO ROC [SEC 64]: If a company alters its share capital in any of the above mentioned ways then the company shall file a notice in the prescribed form (*Form SH-7*) with the ROC within 30 days of such alteration along with a copy of altered MOA.

SIMILAR QUESTIONS:

1. The Directors of Wolters India Ltd. desire to consolidate the share capital (FV=10) and divide the share capital into face value of Rs. 100. Company Key Managerial Staff approached you for an advice. As a Practicing Chartered Accountant advise them?

A. Yes the company can do so.

However, consolidation and division which results in changes in the voting percentage of shareholders shall take effect only if it is approved by the tribunal

2. The Directors of Mars India Ltd. desire to alter capital clause of MOA of their company. Advise them, under the provisions of the Companies Act, 2013 about the ways in which the said clause may be altered and the procedure to be followed for such alteration.

A. Refer the above answer.

[NEW SM-TYK, OLD PM]

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 1)

- 1) The authorised share capital of A Ltd. consists of 1,00,000 shares of Rs. 10 each. The company has already issued 1,00,000 shares. The company intends to issue fresh share capital amounting to Rs. 20 lakhs. Before issuing the fresh shares, the company has to first increase the authorised capital u/s 61(1)(a).
- 2) The authorised share capital of B Ltd. consists of 1,00,000 shares of Rs. 10 each, fully paid up. The company may consolidate and divide the shares u/s 61(1)(b) such that the share capital becomes 10,000 shares of Rupees 100 each, fully paid up.
- 3) The share capital of C Ltd. consists of 1,00,000 shares of Rs. 10 each, fully paid up. The company may convert its fully paid shares into stock u/s 61(1)(c). On such conversion, C Ltd. shall have a stock of Rs. 10 lakhs, Afterwards, C Ltd. may reconvert stock into shares.
- 4) The authorised share capital of D Ltd. consists of 1,00,000 shares of Rs. 10 each, Rs. 5 paid up. The company may sub-divide its shares into shares of smaller amount u/s 61(1)(d) such that the share capital becomes 10,00,000 shares of Rs. 1 each, Re. 0.5 paid up.
- 5) The authorised share capital of E Ltd. consists of 1,00,000 shares of Rs. 10 each. The company issues the whole of the share capital to the public. However, the public subscribes to 96,000 shares only. The company may cancel the balance 4,000 shares which have not been subscribed to by the public.

Q.No.2. When can a Public Company offer the new shares (further issue of shares) to persons other than the existing shareholders of the Company? Can these shares be offered to the Preference Shareholders? (B) (NEW SM, OLD SM, RTP N18 (N&O))

- 1) **ISSUE OF FURTHER SHARES [Section 62]:** At any time, If a company having a share capital intends to increase its subscribed capital by the issue of further shares then such shares shall be offered to following:
- a) Existing equity shareholders of the company as at the date of the offer through a letter of offer subject to certain conditions (*proportion to the capital paid up on those shares - Rights issue*) [Sec 62 (1) (a)].
NOTE: If company offers any shares to its members and members declined such offer then the Board of Directors may dispose the shares in such manner which is not disadvantageous to the shareholders or to the company.
 - b) Employees under a scheme of employees' stock option (ESOP)⁶ subject to
 - i) A special resolution passed by the company and (*for Private companies Ordinary Resolution is sufficient*).
 - ii) Such conditions as may be prescribed [Sec 62(1)(b)].
 - c) Any other persons, either for cash or kind, subject to
 - i) A special resolution
 - ii) Price determination of shares by Registered Valuer subject to the compliance with the applicable provisions of Chapter III
 - iii) Such conditions as may be prescribed [Sec 62(1)(c)].

Exception: Section 62 is not applicable in certain cases - Refer question 4.

- 2) **FURTHER ISSUE OF SHARES:** From the wordings of Sec 62(1) (c), it is quite clear that these shares can be issued to any persons who may be preference shareholders as well provided
- a) Such issue is authorized by a SR of the company and
 - b) Are issued on such conditions as may be prescribed.

SIMILAR QUESTIONS:

1. A company, listed at Bombay Stock Exchange, intends to offer its new shares to the non-members. The existing members of the company consider such offer as invalid in view of the provisions contained in Section 62 (1) (a). However, the company is not prohibited in absolute terms while offering new shares to the non-members. Can the Company do so?

A. It can do so after fulfilling the conditions given in Section 62 (1) (c). Thus, new shares of a company limited by shares may be issued to non-members under certain circumstances.
2. The Board of directors of New Star Ltd. passed a resolution for issue of rights shares. However, certain shareholders of the company raised an objection as to whether the company needed additional capital. Discuss the validity of the counter-move taken by the shareholders and resolution passed by the Board

A. In the case of Aijun Tukaram Shelgaonkar V. Urmila Valkunth, a shareholder had questioned against a resolution of Board of directors in respect of increase in the share capital of the company. The shareholders had the right to raise question because his shareholding was going to be diluted. Further in Needle Industries (India) Ltd. Vs Needle Industries Newey (India) Holding Ltd. (1981) the Court/Tribunal pointed out that for the benefit of the company the directors of the company must exercise their powers. If the directors of the company use their powers for personal interest and not for the benefit of the company, under those circumstances, the Court/Tribunal will interfere and prevent the directors for doing so. Thus the counter move taken by the shareholders is valid.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 2,3)

6) 'Employees' stock option' means the option given to the directors, officers or employees of a company or of its holding company or subsidiary company or companies, if any, which gives such directors, officers or employees, the benefit or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price.

Q.No.3. What are the conditions to be complied for Proportionate offer to existing shareholders [Sec 62(1)(a)]? (B) (NEW SM, OLD SM, OLD PM)

RIGHTS ISSUE:

MEANING: 'Right' refers to the entitlement of existing shareholders to receive invitation of offer or subscription to the shares of a company in case of further issue of capital by the company, before being offered to others. This is called Right of pre-emption.

CONDITIONS:

- 1) **BASIS OF OFFER:** Further shares shall be offered to exiting⁷ equity shareholders, in proportion to the capital paid up on the shares held by them.
- 2) **LETTER OF OFFER:**
 - a) Proportionate offer to existing shareholders shall be made by way of a letter of offer.
 - b) **Contents:** Letter of Offer shall specify that -
 - i) Number of shares offered.
 - ii) Time within which the offer must be accepted by existing members. (Minimum 15 days, Maximum 30 days from the date of offer).
 - c) **Statement:** Letter of offer shall state that -
 - i) The offer shall be deemed to have been declined if it is not accepted within the specified time, and
 - ii) The members have right to renounce all or any of the shares offered to them in favour of any other person unless otherwise provided in the AOA.
- 3) **MODE OF SENDING NOTICE:** Notice shall be sent to existing members, through Registered Post or Speed Post or Electronic mode or courier or any other mode having proof of delivery, at least 3 days before the opening of Issue.
- 4) **SHORTER PERIOD:** In case of Private company, if 90% of the members given consent in writing or in electronic mode then time period given in the following cases can be reduced.
 - a) Rights issue open for minimum of 15 days and maximum of 30 days.
 - b) Letter of Offer is to be sent at least 3 days before opening of the issue.
- 5) BOD may dispose the shares offered in a manner which is not disadvantageous to the shareholders, if
 - b) Time given in notice expires or
 - c) The person denies from accepting the offer.

Q.No.4. Explain the provisions relating to conversion of Debentures issued or loans obtained into Shares [Sec 62]? (B) (NEW SM)

SECTION 62 DOES NOT APPLY TO INCREASE OF SUBSCRIBED CAPITAL CAUSED IN THE FOLLOWING CASES:

- 1) **Conversion of debentures or loans into shares - when option is attached at the time of Issue:**
Nothing in Section 62 shall restrict the power of the company to allot shares on account of conversion of Loans or debentures into shares if the following conditions are satisfied-
 - a) The terms of issue of such debentures or loan containing an option of such conversion in future
 - b) It is approved by a SR passed by the company in GM. Such approval (SR) is obtained before the issue of such debentures or the raising of loan.

7) Existing means as on date of offer

2) Conversion of debentures or loans into shares - On Government direction:**a) CG may make an order that –**

- i) Debentures issued to the Government; or
- ii) Loans obtained from the Government by a Company
- iii) Shall be converted into shares in the company.

b) The Government can order such conversion even if the terms of issue of such debentures or loans did not contain any specific term regarding such conversion in future.

c) In giving such direction the government shall consider the following factors:

- i) Financial Position of the company.
- ii) Terms of issue of debentures or loans
- iii) Rate of Interest payable on debentures or loans
- iv) Other matters as it may consider necessary.

d) **Remedy to company:** However, if the terms and conditions of such conversion are not acceptable to the company then it can file an appeal with tribunal within 60 days of the date of communication of Government order.

e) If no appeal is made by the company or appeal has been dismissed by the tribunal (NCLT) then the -

- i) MOA of the company shall stand altered, and
- ii) The authorized capital of the Company shall stand increased to the extent of converted amount.

3) The company should file a Return u/s 64 for alteration in capital with ROC, within 30 days of receipt of the order from Government.

NOTE: The Provisions of Sec 62 shall not apply for Nidhi companies

SIMILAR QUESTIONS:

1. In the year 2010, Company issued secured non-convertible debentures to the Government for the term of 10 years. In the Year 2020, the company is not in a position to redeem the debentures. On 30.11.2020, Government ordered Company to convert Debentures into Equity Shares. Explain the remedies available to Company.
- A. Refer 3d, 3e above

Q.No.5. Discuss the provisions relating to issue of bonus shares by the Company. (B) (NEW SM)

Bonus shares are shares issued proportionately by a company to its current (Existing) shareholders as fully paid shares free of any cost to them.

MEANING: Bonus share is the share allotted by the company to its member out of its Distributable profits⁸.

1) TYPES OF BONUS ISSUE:

- a) Issuing fully paid up shares to its existing members.
- b) Conversion of partly paid shares into fully paid shares.
- c) Combination of above.

2) **SOURCES FOR BONUS ISSUE:** A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of:

- a) Its free reserves;
- b) The securities premium A/c; or
- c) The capital redemption reserve A/c:

3) **AMOUNTS NOT USABLE:** Issue of Bonus shares shall not be made by capitalizing reserves created by the revaluation of Assets.

8) Example: 1:3 bonus issue means an existing shareholder will get one extra free share for every three shares already held by him/her.

- 4) **CONDITIONS FOR BONUS ISSUE:** Company shall capitalise its profits or reserves for the purpose of issuing fully paid-up bonus shares on satisfaction of following conditions:
- AOA:** Issue of Bonus shares is authorized by the AOA;
 - Recommendation:** It should be recommended by Board of Directors;
 - Ordinary Resolution:** It must be authorised by the shareholders by passing OR in the general meeting.
 - No default in Deposits/ Debt:** The Company has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
 - No default in Employee Statutory Dues:** Company has not defaulted in payment of statutory dues of the employees Ex: contribution to provident fund, gratuity and bonus;
 - Partly Paid up shares:** The partly paid-up shares, if any outstanding on the date of allotment, are to be made fully paid-up;
 - Not in Lieu of Dividend:** The bonus shares shall 'not be issued in lieu of dividend'
 - No Withdrawal:** Company which has announced the Board recommendation of bonus issue, shall not withdraw the same subsequently. [Rule 14 of Company (Share Capital and Debenture) rules, 2014]
 - It complies with other conditions as may be prescribed.
- 5) According to the proviso to Sec.123(5) of the Companies Act, 2013, it is permissible for a company:
- To capitalise its profits or reserves for the purpose of issuing fully paid up bonus shares or
 - Paying up any amount for the time being unpaid on any shares held by the members of the company.

SIMILAR QUESTIONS:

1. MN Ltd. Is engaged in the manufacture of consumer goods and has got a good brand value Over the years, it has a built a good reputation and its Balance Sheet as at March 31, 2007 shows the following position:

Authorized Share Capital (25,00,000 equity shares of face value of Rs 10/- each)	Rs.2,50,00,000
Issued, subscribed and paid-up capital (10,00,000 equity shares of face value of Rs.10/- each)	Rs. 1,00,00,000
Free Reserves	Rs.3,00,00,000

The Board of Directors is proposing to declare a bonus issue of 1 share for every 2 shares held by the existing shareholders. The Board wants to know the conditions and the manner of issuing bonus shares under the provisions of the Companies Act, 2013. Advise. (N17 - 4M, MTP M18(N))

- A. Refer the above answer. Refer the above answer. No, only fully paid up preference shares can be redeemed.
2. The Board of directors of Pooja Ltd., a listed company, at its meeting held on 1st April, 2020 announced a proposal for issue of bonus shares to all equity shareholders of the company at 1:1 ratio. On 1st May, 2020, the directors at another meeting passed a resolution to reverse the proposal of bonus issue announced on 1st April, 2020. Discuss the validity of the proposal and the reversal.
- A. Refer Point 4h above.
- However in view of the above, the proposal to announce the bonus issue made by the Board of Directors is valid but the reversal is not valid. Further the proposal to issue bonus shares may be approved or reversed by the shareholders in general meeting
3. Kaushal was holding 2,000 equity shares in a company on 20th August, 2015 when the shareholders approved the proposal to issue bonus share in the ratio of one equity share for every two shares held on a date to be determined by the Board. The Board determined the date of entitlement as 31st October 2015. Kaushal sold his holdings in the company on 27th August 2015 and claimed bonus shares from the company. Is Kaushal's claim legally tenable?
- A. Hint - not tenable, date of entitlement is of importance
4. BOD of Relyhans Industries Ltd. announced issue of 40,000 bonus shares to preference shareholder as on 1 October 2016 and for the issue it utilized the amount of revaluation reserve i.e. Rs. 6 lakh. Explain whether the action of company is tenable as per provisions of Companies Act, 2013
- A. No the Company's contention is not tenable

A company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—

- i) Its free reserves;
- ii) The securities premium account; or
- iii) The capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 4)

Q.No. 6. Write the cases where the companies are required to file notice of alteration of share capital with the ROC under the Companies Act, 2013. (C) (NEW SM, OLD SM)

NOTICE TO BE GIVEN TO ROC FOR ALTERATION OF SHARE CAPITAL [SEC 64]:

- 1) A company shall give a notice to ROC in case of:
 - a) Alteration of Share Capital u/s 61(1).
 - b) Increase in the authorized share capital consequent to order of CG u/s 62.
 - c) Redemption of preference shares u/s 55
- 2) The company shall file a notice in the prescribed form with the ROC within a period of 30 days of such alteration or increase or redemption, *(as the case may be,)* along with an altered MOA.

PUNISHMENT IN CONTRAVENTION OF THE PROVISION [SEC 64(2)]:

Who is Punishable	PENALTY
Company and Every Officer in default	up to Rs.1,000 for each day of continuing default. <u>or</u> Rs. 5,00,000 whichever is less.

Q.No.7. what are the circumstances under which a company may reduce its share capital? Or List the ways of reduction of capital with sanction of NCLP. (B) (NEW SM, OLD SM, OLD PM)

REDUCTION OF SHARE CAPITAL: Reduction of capital means reduction of issued, subscribed and paid up capital of the company, if so authorised by AOA of the company.

CONDITIONS FOR REDUCTION OF SHARE CAPITAL-

- 1) The company should be limited by shares and Company Limited by Guarantee having Share Capital.
- 2) The reduction should be approved by the Tribunal.
- 3) Special resolution is required to be passed to that effect.
- 4) Company is not in arrears in the repayment of any deposits accepted by it, either before or after the commencement of this Act, or the interest payable thereon.
- 5) MOA of the company shall be altered accordingly.

Modes of Reduction: A company may-

- 1) Extinguish or reduce the liability on any of its shares in respect of the share capital not paid-up⁹; or
- 2) Either with or without extinguishing or reducing liability on any of its shares,—
 - a) cancel any paid-up share capital which is lost or is unrepresented by available assets; or
 - b) pay off any paid-up share capital which is in excess of the wants of the company.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 7)

Copyrights Reserved To **MASTER MINDS COMMERCE INSTITUTE PVT.LTD.**

9) In respect of a share of Rs. 10, a company has called only Rs. 7per share and the same has been paid by all the shareholders. The company decides not to call remaining Rs. 3 per share and reduces its shareholders' liability. If done, the company is said to have reduced its share of Rs. 10 to Rs. 7 as fully paid-up share.

Q.No.8. Describe the formalities to be complied if a company intends to reduce its share capital or State the procedure for reduction of capital. (B) (NEW SM, OLD SM, OLD PM)

PROCEDURE FOR REDUCTION OF SHARE CAPITAL

- 1) **SPECIAL RESOLUTION:** The Company shall pass a special resolution at its GM for reduction of share capital. This is called resolution for reducing share capital.
- 2) **CONFIRMATION BY TRIBUNAL:** Reduction of Share capital shall take effect only when it is confirmed by the Tribunal on an application made by the company.
 - a) **Issue of notice from tribunal:** The Tribunal shall give notice of every application made to it, to the -
 - i) Central Government, ROC and
 - ii) SEBI, in the case of listed companies, and
 - iii) Creditors of the company.
 - b) The Tribunal shall take into consideration the representations, if any, made to it by that Government, ROC, SEBI and the creditors within a period of 3 months from the date of receipt of the notice.
 - c) However, where no representation has been received from the Central Government, ROC', SEBI or the creditors within the said period, it shall be presumed that they have no objection to the reduction.
- 3) **ORDER OF THE TRIBUNAL:** Tribunal confirms the reduction of share capital on satisfaction of following conditions:
 - a) **Creditor claims:** Debt or claim of every creditor of the company
 - i) has been discharged or determined or
 - ii) has been secured or
 - iii) his consent is obtained,
 - b) **Accounting Treatment:**
 - i) The accounting treatment proposed for capital reduction is in conformity with the accounting standards specified u/s 133.
 - ii) A certificate from the company's auditor to the above effect should be filed with the Tribunal.
- 4) **PUBLISHING OF ORDER OF CONFIRMATION OF TRIBUNAL:**
 - a) The Company should publish the Tribunal's order confirming the reduction of share capital, in the manner directed by the Tribunal.
 - b) If a company fails to comply with the above provisions, it shall be punishable with fine which shall not be less than Rs. 5,00,000 but which may extend to Rs. 25,00,000.
- 5) **DELIVERY OF CERTIFIED COPY OF ORDER TO ROC:** Within 30 days of receipt of order, the Company shall deliver to ROC
 - a) A certified copy of Tribunal's order and
 - b) A minute approved by the Tribunal showing
 - c) **Contents of Minutes:**
 - i) Amount of share capital;
 - ii) Number of shares into which it is to be divided;
 - iii) Amount of each share; and
 - iv) Amount deemed to be paid-up on each share at the date of registration.
 - d) ROC shall register the same and issue a certificate to that effect.

6) LIABILITY OF MEMBERS IN RESPECT OF REDUCED SHARES:

- a) Members shall not be liable to any call or contribution, exceeding the amount of difference (if any) between -
 - i) The amount paid on the share, (or reduced amount deemed to be paid thereon, as the case may) and
 - ii) The amount of the share as fixed by the Tribunal order confirming such reduction.
- b) Members shall be liable in the following case:
 - i) **Conditions:**
 - Where a creditor who is entitled to object to the reduction of share capital was not entered in the list by virtue of his ignorance of the proceedings for reduction and
 - Company commits a default, within the meaning of section 6 of the Insolvency and Bankruptcy Code, 2016, in respect of the amount of his debt or claim
 - ii) **Persons Liable:** Every person, who was a member of the company on the date of the registration of order for reduction by the ROC.
 - iii) **Liability:** Payment of that debt or claim, an amount not exceeding the amount which he would have been liable to contribute if the company had gone into liquidation.
 - iv) **If the company is wound up:**

The Creditor may make an application to Tribunal, who shall -

 - settle a list of persons so liable to contribute, and
 - make and enforce calls and orders on the contributories as if they were ordinary contributories in a winding up

7) PENALTY FOR NON-COMPLIANCE:

Who is Punishable	Nature of Default	Punishment
Any officer of the company, who knowingly -	<ul style="list-style-type: none"> • conceals the name of any creditor entitled to object to the reduction or • misrepresents the nature or amount of the debt or claim of any creditor, or • abets or is party to any such concealment or misrepresentation 	liable under section 447
Company	Failure to comply with Publication of Tribunal Order	Fine: Minimum: Rs. 5,00,000 Maximum: Rs. 25,00,000

- 8) **BUY-BACK OF SHARES:** The above provisions shall not apply to buy-back of its own securities by a company u/s 68.

SIMILAR QUESTIONS:

- 1. Red Cap Ltd wants to reduce its equity share capital to extinguish the holding of non-promoter shareholders on payment of value of their shares. Reduction was approved by requisite majority of equity shareholders including non-promoter shareholders. Will such selective reduction be sanctioned?
 - A. Reduction of Share capital shall take effect only when it is confirmed by the Tribunal on an application made by the company.
- For detailed procedure - refer above answer

Q.No.9. Can companies buy its own shares? When a company gives loan or financial assistance to purchase its own shares? (A) (NEW SM, N15 - 5M)

RESTRICTION ON PURCHASE BY COMPANY OR GIVING OF LOANS BY IT FOR PURCHASE OF ITS SHARES [SEC 67]:

- 1) **Restriction on Purchase of its Shares by Company [SEC 67(1)]:** A fundamental principle of Company Law was that a Company cannot buy its own shares [Sec 67(1)].

Applicability to companies: Section 67 is applicable only in case of:

- a) Company Limited by Shares
- b) Company Limited by Guarantee and having Share capital.

2) Company not to finance others for buyback of own securities [Sec 67(2)]:

- a) The provisions are applicable to a public company only.
- b) A public co. shall not, whether directly or indirectly, give to any person a-
 - i) Loan
 - ii) Guarantee
 - iii) Security
 - iv) Any other financial assistance
 For purchase of -
 - i) Its own shares; or
 - ii) Shares in its Holding Company.

3) Exceptions: A company may provide the financial assistance in the following cases:

- a) **Banking Company:** Banking companies lending money in ordinary course of its business;
 - b) **Shares held by Trustees:** The provision of money by a company
 - i) in accordance with any scheme approved by company through special resolution with such requirements as may be prescribed,
 - ii) for the purchase of, or subscription for, fully paid up shares in the company or its holding company,
 - iii) being a purchase of shares by the trustees for the benefit of the employees;
 - c) **Loans to employees:** The giving of loans by a company to persons in the employment of the company other than its directors or key managerial personnel, for an amount not exceeding their salary or wages for a period of 6 months with a view to enabling them to purchase fully paid-up shares in the company or its holding company.
- Board's Report:** Where the voting rights are not exercised directly by the employees in respect of shares to which the scheme relates, the BOD shall disclosure the same in the Board Report in such manner as may be prescribed.
- d) **Non Applicability:** Section 67 is not applicable in the following cases -
 - a) Redemption of Preference Shares u/s 55
 - b) Buy Back of shares u/s 68

4) Exemption to Private Companies:

As per Notification No. G.S.R. 464(E) dated 5th June, 2015, the provisions of Sec. 67 shall not apply if the following conditions are satisfied:

- a) The company is a private company.
- b) No other body corporate has invested any money in the share capital of such private company.
- c) The borrowings of such private company from banks or financial institutions or any body corporate is less than twice its paid up share capital or Rs. 50 crore, whichever is lower.
- d) Such a private company is not in default in repayment of such borrowings subsisting at the time of making any transaction u/s 67.

5) Punishment for Contravention: if a company contravenes the provisions of this section, the punishment shall be as under:

Who Is Punishable	Punishment
Company	Fine: Minimum: 1,00,000; Maximum: 25,00,000
Every officer of the company who is in default	Imprisonment: up to 3 years AND Fine: Minimum: 1,00,000; Maximum: 25,00,000

SIMILAR QUESTIONS:

1. Under what circumstances a company is permitted to buy its own shares or give financial aid to person whether by way of loan, guarantee, or surety or otherwise, purchase or subscription of its own shares or of its holding company?
 - A. Refer above answer
2. A Company wants to provide financial assistance to its employees to enable them to subscribe for fully paid shares of the company. Does it amount to purchase of its own shares. If, in the instant case, the company itself purchasing to redeem its preference shares, does it amount to acquisition of its own shares? (OLD PM)
 - A. Yes. Refer the point 3'c' in exceptions and sec 68.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 8,12)

Q.No.10. State the sources of funds that can be utilised by the company for purchasing its own shares. (A) (NEW SM, OLD SM)

SOURCES OF FUNDS FOR BUY BACK OF SHARES [SEC 68(1)]: A company can purchase its own shares or other specified securities¹⁰ out of:

- 1) Its free reserves; or
- 2) The securities premium A/c; or
- 3) The proceeds of the issue of any shares or other specified securities.

However, No buyback shall be made of eligible securities out of proceeds of an earlier issue of same kind of eligible security.

SIMILAR QUESTIONS:

1. A Public Company proposes to purchase its own shares. State the source of funds that can be utilised by the Company for purchasing its own shares (OLD PM)
 - A. Refer the above answer.
2. ADJ Company Limited decides to buy-back its own shares. Advise the company's BOD about the sources out of which the company can buy-back its own shares. (OLD PM, RTP M16)
 - A. Refer the above answer.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 11)

Q.No.11.What are the Requirements to be Complied for buyback of shares by the company. (A) (NEW SM, OLD SM, N13 - 8M, N16 - 4M)

REQUIREMENTS TO BE COMPLIED WITH, BEFORE BUY - BACK:

- 1) **Conditions for buy-back [Sec.68(2)]:** The company shall purchase its own shares or other specified securities on satisfaction of following conditions:
 - a) **AOA:** The buy-back is authorised by AOA of the company;
 - b) **Resolution:**
 - i) **BR:** Pass Board Resolution, if the buy-back of shares is not more than^(≤) 10% of the aggregate of
 - Total paid up equity capital and
 - Free reserves of the company (including Securities Premium).
 - ii) **SR:** SR is to be passed if the buy-back is more than 10% of the aggregate of total paid up equity capital and free reserves of the company (including Securities Premium)
 - c) **Limit of BUY BACK:**
 - i) **In total:** The buy-back should not exceed 25% of the aggregate of
 - Paid-up capital (both equity and preference) and
 - Free reserves of the company (including Securities Premium);

10) "Specified securities" includes employees' stock option or other securities as may be notified by the CG from time to time.

- ii) **Only equity capital:** Further the buy-back of equity shares in
- Any financial year shall not exceed
 - 25% of its total paid up equity capital in that financial year.
- d) **Post buy-back debt equity ratio:** The ratio of the
- i) Aggregate debts (secured and unsecured) owed by the company
 - ii) After buy back
 - iii) Is not more than twice the paid up capital and its free reserves (including Securities Premium). (2:1)
- Provided that the CG may prescribe a higher ratio of the debt to capital and free reserves for a class or classes of companies;
- Debt to capital and free reserves to NBFC:** The CG has notified that the debt to capital and free reserves ratio shall be 6:1 for government companies which carry on Non-Banking Finance Institution activities and Housing Finance Activities.
- e) **Fully Paid up:** all the shares or other specified securities for buy-back are fully paid-up;
- f) **Compliance of Rules and regulations:**
- i) **Listed:** the buy-back of the shares or other specified securities listed on any recognised stock exchange is in accordance with the SEBI regulations
 - ii) **Unlisted:** the buy-back in respect of shares or other specified securities other than those specified in above (*listed*) is in accordance with rules as may be prescribed. [*i.e. Companies (Share capital and Debentures) Rules, 2014.*]
- g) **Time Gap between 2 buy backs:** No offer of buy-back shall be made within a period of 1 year from the date of the closure of the preceding offer of buy-back, if any.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 9,10)

Q.No.12.What is the procedure to be followed before buyback of shares by the company.

(A) (NEW SM, OLD SM, N13 - 8M, N16 - 4M)

PROCEDURE TO BE FOLLOWED BEFORE BUY BACK:

- 1) **EXPLANATORY STATEMENT [SEC. 68(3)]:** The notice of the meeting at which SR is proposed to be passed shall be accompanied by an explanatory statement stating -
 - a) A full and complete disclosure of the all material facts;
 - b) The necessity for the buy-back;
 - c) The class of shares or securities intended to be purchased under the buy back;
 - d) The amount to be invested under the buy-back; and
 - e) The time limit for completion of buy-back.
- 2) **TIME LIMIT FOR COMPLETION OF BUY-BACK [SEC. 68(4)]:** Every buy-back shall be completed within 12 months from the date of
 - a) Passing the SR at GM or
 - b) A Board resolution (*BR*) in BM for authorising the buy-back.
- 3) **BUY-BACK FROM WHOM? [SEC. 68(5)]:** The buy-back referred u/s 68 (1) may be -
 - a) From the existing share holders or security holders on a proportionate basis; or
 - b) From the open market; or
 - c) By purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

- 4) **DECLARATION OF SOLVENCY (D.O.S) [SEC. 68(6)]:** Only a solvent company is permitted to buy-back its shares. Before making such buy-back, it shall file an Affidavit to the effect that -
- The Board has made a full inquiry into the affairs of the company and
 - Formed an opinion that it is capable of meeting its liabilities and
 - Will not rendered insolvent within 1 year of date of D.O.S and
 - Signed by at least 2 directors, one of whom shall be MD, if any.
- 5) **FILING WITH ROC AND SEBI:** The Company shall file with the ROC (also SEBI, in case of listed companies), a D.O.S in a prescribed form and verified by an affidavit.

SIMILAR QUESTIONS:

- What are the requirements to be complied with by the Company under the Companies Act before and after the shares are so purchased. (OLD PM)
A. Refer the above answer.
- What conditions are attached to the buy-back scheme of the company in accordance with the provisions of the Companies Act, 2013? Whether there is any time limit for the completion of buy-back of its shares? Explain. (OLD PM, RTP M16)
A. Refer the above answer.
- Xgen Limited has a paid-up capital and free reserves to the extent of Rs.50,00,000. The Company is planning to buy-back shares to the extent of Rs.4,50,000. The Company approaches you for advice with regard to the following:
 - Is special resolution required to be passed ?
 - What is the time limit for completion of buy-back ?
 - What should be ratio of Aggregate debts to the paid-up capital and free reserves after buy-back? (RTP N18 (O), M18(N) - 3M)
 A. Refer the above answer.

(IMMEDIATELY REFER PRACTICAL QUESTION NO. 5, 6)

Q.No.13. What are the Consequences to a company if default in complying with the provision of this section or any regulations made by SEBI to be Complied with before and after the Shares are so Purchased. (A) (NEW SM, OLD SM)

PENALTY FOR DEFAULT: If a company makes default in complying with the provisions of this section or any regulations made by SEBI, then Penalty on

Company with fine	Minimum 1 Lakh	Maximum 3 Lakhs
Every officer with fine or	Minimum 1 Lakh	Maximum 3 Lakhs
Every officer with imprisonment upto 3 years or Both		

Q.No.14. State the provisions relating to requirements to be complied with after buy back. (B) (NEW SM, OLD SM)

REQUIREMENTS TO BE COMPLIED WITH, AFTER BUY - BACK:

- Extinguishment of Physical Securities [Sec. 68(7)]:** The securities bought back should be extinguished and physically destroyed within 7 days after completion of buy-back.
- Cooling period / Prohibition on further issue of similar securities [Sec. 68(8)]:** After completion of buy-back, a company cannot issue same kind of shares or security (*which was bought back*) for a period of 6 months. Allotment of rights issue renounced by members is also not permissible in this period. However, following are permitted:
 - Issue of security of a different class that is other than one which was bought back,
 - Bonus issue,
 - Subsisting obligations such as conversion of warrants,

- d) Stock option to employees
 - e) Sweat equity
 - f) Conversion of preference shares or debentures into equity shares.
- 3) **Register of Buy-back [Sec. 68(9)]:** The company should maintain a register showing
- a) Securities bought back and
 - b) Consideration paid for the bought-back,
 - c) Date of cancellation of securities, date of extinguishment and physical destruction of securities other prescribed particulars.
- 4) **Return of Buyback [Sec. 68(10)]:** After completion of buy-back, a return has to be filed with the ROC and SEBI, if the company is listed within 30 days giving details as prescribed.
- 5) **Capital Redemption Reserve A/c [Sec. 69(1)]:** If the buy-back is from free reserves, a sum equal to the nominal value of Shares purchased will be transferred to CRR A/c. Details of such transfer will be disclosed in the balance sheet of the company.
- 6) The capital redemption reserve account may be applied by the company, in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares. **[Sec. 69(2)]**

Q.No.15. State the legal provisions in respect of 'Declaration of Solvency', which an unlisted public company needs to adhere to while taking steps to buy-back its own shares. **(NEW SM-TYK)**

APPLICABILITY: Where an unlisted public company has passed

- 1) a special resolution u/s 68 (2) (b) or
- 2) the Board has passed a resolution under item (ii) of the proviso to Section 68 (2) (b)

to buy-back its own shares, it shall, before making such buy-back, file with the Registrar a 'Declaration of Solvency' in Form SH-9 [Sec 68 (6)].

DECLARATION:

- 1) The declaration shall be verified by an affidavit to the effect that –
 - a) the Board has made a full inquiry into the affairs of the company as a result of which they have formed an opinion that it is capable of meeting its liabilities and
 - b) will not be rendered insolvent within a period of one year from the date of declaration of solvency adopted by the Board.
- 2) The declaration shall be signed by at least two directors of the company, one of whom shall be the managing director, if any.

Q.No.16. State the provisions of the Companies Act, 2013 relating to "Prohibiting Buy back of shares"? **(B) (NEW SM, M-19(N))**

PROHIBITION FOR BUY-BACK IN CERTAIN CIRCUMSTANCES (SEC 70):

A company cannot buy-back its -

- 1) Shares or
- 2) Other specified securities, directly or indirectly-
 - a) Through any subsidiary company including its own subsidiaries; or
 - b) Through investment or group of investment companies; or
 - c) When the company has defaulted in the
 - i) repayment of deposits or interest thereon,
 - ii) redemption of debentures or

- iii) redemption of preference shares or
- iv) payment of dividend to any shareholder or
- v) repayment of any term loan or interest thereon to any financial institution or bank.

3) **Remedy:** However, buy back is not prohibited if the default has been remedied and 3 years has elapsed after such default ceased to subsist.

OTHER PROHIBITIONS: No company shall directly or indirectly purchase its own shares or other specified securities in case such company has not complied with sec(s) 92, 123, 127 & 129 of the Companies Act, 2013.

NOTE: Description of above specified sec(s):

- 1) filing of Annual return (sec 92),
- 2) Declaration of dividend (sec 123) or
- 3) Punishment for failure to distribute dividend (sec 127) and
- 4) Financial *statements* (sec 129)

SIMILAR QUESTION:

1. Elucidate the circumstances in which a company cannot buy back its own shares as per the provisions of the Companies Act, 2013. M/s Growmore Pharma Limited is planning to buyback of its shares during the current year but the company has defaulted in the payment of term loan & interest thereon to its bankers. The company seeks your advice as to how and when the company can buy back its shares under the provisions of the Companies Act, 2013.

(OLD PM, N14 - 4M)

A. No. M/s. Growmore Pharma Limited needs to follow the above procedure for buy-back of its shares.

SECTION 2: QUESTIONS FOR ACADEMIC INTEREST FOR STUDENTS SELF STUDY

Q.No.1. Discuss the provisions relating to issue of Shares under Employee Stock Options.

(B) (NEW SM)

DEFINITION [SECTION 2(37)]: 'Employee's stock option' means the option given to the directors, officers or employees of a company or of its holding company or subsidiary company or companies, if any, which gives such directors, officers or employees, the benefit or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price.

PROVISIONS CONTAINED IN RULE 12 OF THE COMPANIES (SHARE CAPITAL AND DEBENTURES) RULES, 2014 W.R.T. EMPLOYEE STOCK OPTIONS

1) **Requirement of SR:**

- a) The issue of Employees Stock Option Scheme shall be approved by the shareholders of the company by passing SR
- b) The company shall make the specified disclosures in the explanatory statement annexed to the notice for passing of the resolution

2) **Exercise price:** A company granting option to its employees pursuant to Employees Stock Option Scheme will have the freedom to determine the exercise price in conformity with the applicable accounting policies, if any

3) **Time gap:** There shall be a minimum period of 1 year between the grant of options and vesting of option

4) **Lock in:** The Company shall have the freedom to specify the lock-in period for the shares issued pursuant to exercise of option.

5) **Eligibility:** An employee shall be eligible for grant of option under the Employees Stock Option Scheme, only if he is-

- a) a permanent employee of the company who has been working in India or outside India; or
- b) a director of the company, whether a whole time director or not but excluding an independent director, or

- c) an employee as defined in clauses (a) or (b) of a subsidiary, in India or outside India, or of a holding company of the company, but does not include -
- i) an employee who is a promoter or a person belonging to the promoter group; or
 - ii) a director who either himself or through his relative or through any body corporate, directly or indirectly, holds more than 10% of the equity shares of the company.

However, in case of a startup company, as defined in notification number G.S.R. 127(E), dated 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry Government of India, Government of India, the conditions mentioned in sub-clause (i) and (ii) shall not apply up to 10 years from the date of its incorporation.

TERMS OF ESOS:

- 1) **Exercise Price:** The Companies granting option to its Employees pursuant to ESOS, will have the freedom to determine the Exercise Price in conformity with the applicable accounting policies, if any.
- 2) **Grant to Vesting Time Period:**
 - a) There shall be a minimum period of 1 year between the grant of options and vesting of option.
 - b) In case of Merger or Amalgamation, the period during which the options granted by the Merging or Amalgamating Company were held by the Employee shall be adjusted against the minimum vesting period of 1 year.
- 3) **Lock in Period:** The Company shall have the freedom to specify the lock-in period for the Shares issued pursuant to exercise of option.
- 4) **No Rights till Issue of Shares**
Till Shares are issued on exercise of option, the Employees shall not have right -
 - a) to receive any dividend, or
 - b) to vote, or
 - c) in any manner enjoy the benefits of a Shareholder in respect of Options granted to them.
- 5) **Treatment of amounts received**
Amount payable, if any, by the Employees at the time of grant of option may be -
 - a) forfeited by the Company if the option is not exercised by the Employees within the exercise period, or
 - b) refunded to the Employees if the options are not vested due to non-fulfillment of conditions relating to vesting of option as per the ESOS.

VESTING CONDITIONS OF ESOS:

- 1) **Not Transferable:**
 - a) The option granted to Employees shall not be transferable to any other person.
 - b) No person other than the Employees to whom the option is granted shall be entitled to exercise the option. (**Exception:** in case of death of Employee)
- 2) **No Alienation:** The option granted to the Employees shall not be pledged, hypothecated, mortgaged or otherwise encumbered or alienated in any other manner.
- 3) **Death of Employee:** In the event of the death of Employee while in employment, all the options granted to him till such date shall vest in the Legal Heirs or Nominees of the Deceased Employee.
- 4) **Permanent Incapacity:** If the Employee suffers a permanent Incapacity while in employment, all the options granted to him as on the date of permanent incapacitation, shall vest in him on that day.
- 5) **Resignation / Termination:**
 - a) In case of resignation or termination of employment, all options not vested in the Employee as on that day shall expire.
 - b) The Employee can exercise the options granted to him which are vested within the period specified in this behalf, subject to terms and conditions under the scheme granting such options as approved by the Board.

Q.No.2. Distinguish between the following: ‘Sweat Equity’ and ‘Employee’s Stock Purchase Scheme’.

(C)

Distinction between Sweat Equity and Employees Stock Purchase Scheme (Table Format):

Sweat Equity	Employees Stock Purchase Scheme (ESPS)
It is issued to employees or directors for providing known how or intellectual property rights to company.	There is no such consideration in case of ESPS.
Lock-in period of 3 years applicable to sweat equity.	Lock-in period of 1 year is applicable.
Sweat equity can be issued to promoters.	ESPS cannot be issued to promoters.

Q.No.3. Every Employee of a Company shall be Eligible to Participate in ESOS?

(C)

- 1) Every Employee is eligible to participate in Employees Stock Option Scheme (ESOS).
- 2) An Employee who is promoter or belongs to promoters group, shall not eligible to participate in the ESOS.
- 3) Director, who either by himself or through his relative or through anybody corporate, directly or indirectly hold more than 10% of the outstanding equity shares of the Company shall not be eligible to participate into ESOS.

SECTION 3: PRACTICAL QUESTIONS FOR CLASSROOM DISCUSSION

Q.No.1. A Limited has an Authorized Capital of 10,00,000 equity shares of the face value of 100/- each. Some of the shareholders expressed their opinion in the Annual General Meeting that it is very difficult for them to trade in the shares of the company in the share market and requested the Company to reduce the face value of each share to 10/- and increase the number of shares to 1,00,00,000. Examine whether the request of the shareholders is possible and if so, how the company can alter its share capital as per the provisions of the Companies Act 2013. **(Nov’ 17)**

PROVISION: As per section 61 of the Companies Act, 2013, a limited company having share capital may alter its memorandum so as to

- divide all or any of its share capital of a larger amount than its existing shares or
- sub-divide the whole or any part of its shares of smaller amount than is fixed by the memorandum

However the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same as it was before such division or sub-division. For such alteration the company

- i) must be authorized by its articles
- ii) must pass an ordinary resolution in the general meeting.
- iii) shall alter its memorandum
- iv) shall file a copy of the altered memorandum with the Registrar.

ANALYSIS & CONCLUSION: In the given instance, shareholders of A Limited in the Annual General Meeting, requested the company to reduce the face value of each shares from 100 to 10 per share and increase the number of shares, than is fixed by the memorandum from 10 lacs to 1 crore. According to the provision of the Act it is possible for the company to sub-divide the shares provided it is authorised by its articles.

Q.No.2. Shyam Dairy Ltd., a dairy products manufacturing company wants to set-up a new processing unit at Jaipur. Due to paucity of funds, the existing share holders are not willing to fund for expansion. Hence, the Company approached XYZ Ltd. For subscribing to the shares of the Company for expansion purposes. Can Shyam Dairy Ltd. issue shares only to XYZ Ltd. Under the provisions of the Companies Act, 2013? If so. State the conditions. **(N17 - 4M, MTP1 M18 (N))**

PROVISIONS: According to Section 62 of the Companies Act, 2013 if at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares should be offered to the existing equity shareholders of the company as at the date of the offer, in proportion to the capital paid up on those shares. If the existing shareholders refuse to take up the shares the Board may dispose the shares in any manner they deem fit which is not disadvantageous to the shareholders or the company.

ANALYSIS AND CONCLUSION: In the above case Shyam Dairy Ltd. wanted to set up a new unit and was in need of capital for the same. The existing shareholders refused to take up the shares due to paucity of funds. The company approached XYZ Ltd. to subscribe for the shares of the company. As the members had refused to take up the shares of the company the Board may offer the shares to any person if it is not disadvantageous to the shareholders or the company.

Thus Shyam Dairy Ltd. may offer the shares to XYZ Ltd.

Q.No.3. VRS Company Ltd. is holding 45% of total equity shares in SV Company Ltd. The BOD of SV Company Ltd. (incorporated on January 1, 2014) decided to raise the share capital by issuing further Equity shares. The BOD resolved not to offer any shares to VRS Company Ltd., on the ground that it was already holding a high % of the total number of shares already issued, in SV Company Ltd. The Articles of Association of SV Company Ltd. provides that the new shares be offered to the existing shareholders of the company. On March 1, 2014 new shares were offered to all the shareholders except VRS Company Ltd. Referring to the provisions of the Co Act, 2013 examine the validity of the decision of the BOD of SV Company Limited of not offering any further shares to VRS Company Limited. **(NEW SM - TYK, OLD PM, M17- 5M)**

PROVISIONS OF LAW: As per the sec 62 of the Co Act, 2013, where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to:

Persons who, at the date of the offer, are holders of equity shares of the company in proportion, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely:

The company cannot ignore a section of the existing shareholders and must offer the shares to the existing equity shareholders in proportion to their holdings.

RELEVANT CASE LAW: Gas Meter Ltd. Vs Diaphragm & General leather Co. Ltd

The facts of the case were similar to those given in the present case, the AOA of Diaphragm Company provided that the new shares should first be offered to the existing share holders. However, the company offered new shares to all shareholders excepting Gas Co., which held its controlling shares. It was held that Diaphragm Company had no legal authority under the Companies Act to do so.

ANALYSIS AND CONCLUSION: Applying the provisions and the ruling in the above case, SV Ltd.'s decision not to offer any further shares to VRS Co. Ltd on the ground that VRS Co. Ltd already held a high percentage of shareholding in SV Co. Ltd. is not valid for the reason that it is in violation of the provisions of Sec 62 of the Companies Act, 2013.

Q.No.4. Shankar Portland Cement Limited is engaged in the manufacture of different types of cements and has got a good brand value. Over the years, it has built a good reputation and its Balance Sheet as at March 31, 2020 showed the following position:

- a) Authorized Share Capital (25,00,000 equity shares of Rs. 10/- each) Rs. 2,50,00,000
- b) Issued, subscribed and paid-up Share Capital (10,00,000 equity shares of Rs. 10/- each, fully paid-up) Rs. 1,00,00,000
- c) Free Reserves Rs. 3,00,00,000

The Board of Directors are proposing to declare a bonus issue of 1 share for every 2 shares held by the existing shareholders. The Board wants to know the conditions and the manner of issuing bonus shares under the provisions of the Companies Act, 2013. **(NEW SM-TYK)**

According to Section 63 of the Companies Act, 2013, a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of -

- a) its free reserves;
- b) the securities premium account; or
- c) the capital redemption reserve account.

However, no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.

CONDITIONS FOR ISSUE OF BONUS SHARES: No company shall capitalise its profits or reserves for the purpose of issuing fully paid-up bonus shares, unless—

- a) it is authorised by its Articles;
- b) it has, on the recommendation of the Board, been authorised in the general meeting of the company;
- c) it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;
- d) it has not defaulted in respect of payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;
- e) the partly paid-up shares, if any, outstanding on the date of allotment, are made fully paid-up;
- f) it complies with such conditions as are prescribed by Rule 14 of the Companies (Share Capital and debentures) Rules, 2014 which states that the company which has once announced the decision of its Board recommending a bonus issue, shall not subsequently withdraw the same.

Further, the company has to ensure that the bonus shares shall not be issued in lieu of dividend.

For the issue of bonus shares Shankar Portland Cement Limited will require reserves of Rs. 50,00,000 (*i.e.* half of Rs. 1,00,00,000 being the paid-up share capital), which is readily available with the company. Hence, after following the above conditions relating to the issue of bonus shares, the company may proceed for a bonus issue of 1 share for every 2 shares held by the existing shareholders.

Q.No.5. Mars India Ltd. owed to Sunil Rs. 1,000. On becoming this debt payable, the company offered Sunil 10 shares of Rs. 100 each in full settlement of the debt. The said shares were fully paid and were allotted to Sunil. Examine the validity of this allotment in the light of the provisions of the Companies Act, 2013. **(NEW SM - TYK, OLD PM, MTP1 N18 (N))**

PROVISIONS: U/s 62 (1) (c) of the Companies Act, 2013 where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, either for cash or for a consideration other than cash, such shares may be offered to any persons, if it is authorised by a SR and if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as may be prescribed.

ANALYSIS: In the present case, Mars India Ltd is empowered to allot the shares to Sunil in settlement of its debt to him. The issue will be classified as issue for consideration other than cash must be approved by the members by a SR. Further, the valuation of the shares must be done by a registered valuer.

CONCLUSION: Thus Mars Ltd. can allot the shares to Sunil in full settlement of the debt provided it had passed a special resolution and the shares are valued by a registered valuer, subject to the compliance with the applicable provisions of Chapter III and any other conditions as may be prescribed.

Q.No.6. X Ltd. issued a notice on 1st Feb, 2018 to its existing shares holders offering to purchase one extra share for every five shares held by them. The last date to accept the offer was 15th Feb, 2018 only. Mr. Kavi has given an application to renounce the shares offered to him in favour of Mr. Ravi, who is not a shareholder of the company. Examine the validity of application of Mr. Kavi under the provisions of the Companies Act, 2013. Would your answer differ if Mr. Kavi is a shareholder of X Ltd.? **(N19 (N))**

PROVISION: According to section 62 of the Companies Act, 2013, where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely:-

- a) the offer shall be made by notice specifying the number of shares offered and limiting a time not being less than fifteen days and not exceeding thirty days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined;
- b) unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person; and the notice referred to in clause (i) shall contain a statement of this right;

- c) after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the Board of Directors may dispose of them in such manner which is not dis-advantageous to the shareholders and the company.

ANALYSIS AND CONCLUSION: In the instant case, X Ltd. issued a notice on 1st Feb, 2018 to its existing shares holders offering to purchase one extra share for every five shares held by them. The last date to accept the offer was 15th Feb, 2018 only. Mr. Kavi has given an application to renounce the shares offered to him in favour of Mr. Ravi, who is not a shareholder of the company.

As nothing is specified related to the Articles of the company, it is assumed offer shall be deemed to include a right of renunciation. Hence, Mr. Kavi can renounce the shares offered to him in favour of Mr. Ravi, who is not a shareholder of the company.

In the second part of the question, even if Mr. Ravi is a shareholder of X Ltd. then also it does not affect the right of renunciation of shares of Mr. Kavi to Mr. Ravi.

Q.No.7. ABC Ltd. has following balances in their Balance Sheet as on 31st March, 2018:

Equity shares capital (3.00 lakhs equity shares of 10 each)	30.00 lakhs
Free reserves	05.00 lakhs
Securities Premium Account	03.00 lakhs
Capital redemption reserve account	04.00 lakhs
Revaluation Reserve	03.00 lakhs

Directors of the company seeks your advice in following cases:

Whether company can give bonus shares in the ratio of 1:3?

What if company decide to give bonus shares in the ratio of 1:2?

(Nov' 18)

PROVISION: As per Section 63 of the Companies Act, 2013 a company may issue fully paid-up bonus shares to its members out of—

- its free reserves;
- the securities premium account; or
- the capital redemption reserve account:

Issue of bonus shares shall not be made by capitalizing reserves created by the revaluation of assets.

ANALYSIS AND CONCLUSION: In the given case ABC Ltd. has issued 3,00,000 equity shares of 10 each. The company proposes to issue bonus shares. The total amount of fund available for such issue is 12 lakhs (i.e. 5.00+3.00+4.00). So the company can issue bonus shares upto the value of 12 lakhs.

- For issue of bonus shares in the ratio of 1:3 the total fund required shall be 10 lakhs (1/3 of 30.00 lakh) which is well within the limit of available amount of ` 12 lakhs. So, ABC Limited can go ahead with the bonus issue in the ratio of 1:3.
- In case ABC Limited intends to issue bonus shares in the ratio of 1:2, there will be a requirement of 15 lakhs ($\frac{1}{2} \times 30.00$ lakh). Here in this case, the company cannot go ahead with the issue of bonus shares in the ratio of 1:2, since the requirement of 15 Lakhs is exceeding the available eligible amount of 12 lakhs.

Q.No.8. A public limited company having a paid up share capital of Rs 20 lakhs divided in 20,000 shares of Rs 100 each wants to reduce its capital to Rs 15 lakhs by converting the equity share of Rs100 each to Rs 75 each. Can the company do so? Advice the company.

PROVISION: As per Section 66(1), a company limited by shares if authorised by its articles, may reduce its capital by adopting the following procedure.

- by passing a special resolution for reduction of capital, and
- by obtaining confirmation of Tribunal.

ANALYSIS AND CONCLUSION: In the present case, it is to be seen whether the company is authorised by its articles to reduce the share capital. If not so authorised, then first the articles should be amended so as to authorise the company for reduction of share capital. Then, the company can reduce its share capital by passing a special resolution for the reduction of the capital and then applying to The National Company Law Tribunal for an order confirming the reduction of capital.

Q.No.9. OLAF Limited, a subsidiary of PQR Limited, decides to give a loan of ` 4,00,000 to its Human Resource Manager Mr. Surya Nayan, who does not fall in the category of Key Managerial Personnel and draws a salary of ` 40,000 per month, to buy 500 partly paid-up equity shares of ` 1000 each in OLAF Limited. Examine the validity of company's decision under the provisions of the Companies Act, 2013.

[NEW SM-TYK]

RESTRICTIONS ON PURCHASE BY COMPANY OR GIVING OF LOANS BY IT FOR PURCHASE OF ITS SHARE: As per section 67 (3) of the Companies Act, 2013 a company is allowed to give a loan to its employees subject to the following limitations:

- a) The employee must not be a director or Key Managerial Personnel;
- b) The amount of such loan shall not exceed an amount equal to six month's salary of the employee.
- c) The loan must be extended for subscribing fully paid-up shares.

ANALYSIS AND CONCLUSION: In the given instance, Human Resource Manager Mr. Surya Nayan is not a Key Managerial Personnel of the OLAF Limited. Further, he is drawing a salary of Rs. 40,000 per month and wants to avail loan for purchasing 500 partly paid-up equity shares of Rs. 1000 each of OLAF Limited in which he is employed.

Keeping the above facts and legal provisions in view, the decision of OLAF Limited in granting a loan of Rs. 4,00,000 for purchase of its partly paid-up shares to Human Resource Manager is invalid due to the following reasons:

- a) The amount of loan is more than 6 months' salary of Mr. Surya Nayan, the HR Manager. It should have been restricted to Rs. 2,40,000 only.
- b) The loan to be given by OLAF Limited to its HR Manager Mr. Surya Nayan is meant for purchase of partly paid shares.

Q.No.10. DJA Company Ltd., desired of buying back of all its equity shares from the existing shareholders of the company, seeks your advice. Examining the provisions of the Companies Act, 2013 advise whether the above buy back of equity shares by the company is possible. Also state the sources out of which buy- back of shares can be financed.

(OLD PM, RTP M18 (N))

PROVISIONS OF LAW: Sec 68 of the Companies Act, 2013 - Power of company to purchase its own securities.

ANALYSIS: As per sec 68 of the Companies Act, 2013

Maximum Limit for buy back is as follows:

- a) **In total:** The buy-back is 25% or less of the aggregate of paid-up capital (*both equity and preference*) and free reserves of the company;
- b) **For equity capital:** Further the buy-back of equity shares in any financial year shall not exceed 25% of its total paid up equity capital in that financial year.

Whatever may be the case a company cannot buy back its entire equity shares from its existing shareholders.

CONCLUSION: Buying back of all its equity shares from the existing shareholders of the company is not possible.

SOURCES OF BUY BACK: Sec 68(1) of the Companies Act, 2013 specifies the sources of funding buy back of its shares and other specified securities as under:

- a) Free reserves or
- b) Security Premium A/c or
- c) Proceeds of the issue of any shares or other specified securities

However, under the proviso to sec 68(1) no buy back of shares or any specified securities can be made out of the proceeds of an earlier issue of the same kind of shares or same kind of specified securities.

Q.No.11. ABC Company Limited at a GM of members of the Company pass an ordinary resolution to buy-back 30% of its Equity Share capital. The articles of the Company empower the Company for buy-back of shares. The Company further decide the payment for buy-back to be made out of the proceeds of the Company's earlier issue of equity shares. Explaining the provisions of the Companies Act, 2013, and stating the sources through which the buy-back of Companies own shares be executed. Examine.

- a) Whether Company's proposal is in order?
- b) Would your answer be still the same in case the Company instead of 30% decide to buy-back only 20% of its Equity Share Capitals.

(Or)

German Pharmaceuticals Limited is a zero debt company having 10 lakhs Equity shares of Rs.10 each. The Directors desire to buy back its own shares. Can it do so? If so, how? (N-19(N))

PROVISIONS OF LAW: Sec 68 - Power of company to purchase its own securities.

ANALYSIS: As per Sec 68 of the Companies Act, 2013

SOURCES OF FUNDS FOR BUY-BACK OF SHARES: A company can purchase its own shares or other specified securities. The purchase should be out of:

- a) Its free reserves; or
- b) The securities premium A/c; or
- c) The proceeds of the issue of any shares or other specified securities.

However, buy-back of any kind of shares or other specified securities cannot be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities [Sec 68(1)].

CONDITIONS FOR BUY-BACK: The company shall not purchase its own shares or other specified securities unless:

- a) **AOA:** the buy-back is authorised by its articles;
- b) **SR:** a special resolution authorising the buy-back is passed in GM of the company;

MAXIMUM LIMIT FOR BUY BACK IS AS FOLLOWS

- a) **In total:** The buy-back is 25% or less of the aggregate of paid-up capital (both equity and preference) and free reserves of the company.
- b) **For equity capital:** Further the buy-back of equity shares in any financial year shall not exceed 25% of its total paid up equity capital in that financial year.

CASE 1:

- a) The company passed "OR" instead of "SR".
- b) The company proposes to buy back 30% of equity share capital which exceeds the statutory ceiling of 25% of total paid up equity capital.
- c) The company proposes to buy back out of the proceeds of an earlier issue of same kind of shares which is prohibited.

CASE 2:

- a) The company passed "OR" instead of "SR" as required.
- b) The company proposes to buy back 20% of equity share capital which is within statutory limit of 25% of total paid up equity capital.
- c) The company proposes to buy back out of the proceeds of an earlier issue of same kind of shares which is prohibited.

CONCLUSION: The proposal of the company to buy back its shares is not valid in both the cases.

Q.No.12. Binoy, an employee of National Bank Private Limited which is actively engaged in Banking business, drawing a salary of Rs.50,000 p.m., borrowed Rupees One lakh and invested in the shares of the bank. Explain whether there is any violation in the light of the provisions of the companies Act, 2013. would your answer be different if Binoy is a key managerial personnel of the bank. [N19 (O)]

PROVISIONS OF LAW: As per section 67 (3) of the Companies Act, 2013 a public company is allowed to give a loan to its employees subject to the following limitations:

- a) The employee must not be a directors or Key Managerial Personnel;
- b) The amount of such loan shall not exceed an amount equal to six months' salary of the employee.
- c) The shares to be subscribed must be fully paid shares.

ANALYSIS AND CONCLUSION: In the given instance, Binoy is an employee of National Bank Private Ltd. drawing salary of ₹ 50,000 per month, borrowed ₹ 1 lakh and invested in the shares of the bank. On the basis of the above provisions, Mr. Binoy is entitled for the loan from the Bank upto ₹ 3 lakh. Being amount of loan less than his 6 months' salary, considering in compliance with other requirements, there is no violation of the provisions of the Companies Act, 2013. In case, if Mr. Binoy is a Key managerial personnel of the Bank, there will be violation to the provision of law contained in section 67(3) of the Companies Act, 2013.

[NOTE: The above answer is based on the assumption that "National Bank Private Limited" is a public company. Answer may also be given considering "National Bank Private Limited" is a private company.]

SECTION 4: PRACTICAL QUESTIONS FOR STUDENTS SELF PRACTICE

Q.No.1. The Directors of Vijay Electronics Ltd. allotted to themselves certain right shares for which no application was made by certain shareholders as required by Sec 62 of the Companies Act, 2013. Discuss the validity of their action specially in view of the fact that market price of shares of the Company is 50% above par?

PROVISIONS OF LAW: Sec 62 of the Companies Act, 2013 - Further issue of capital.

ANALYSIS: As per the sec 62 of the Companies Act, 2013 where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares; such shares shall be offered to:

Persons who, at the date of the offer, are holders of equity shares of the company in proportion, to the paid-up share capital on those shares by sending a letter of offer subject to the following conditions, namely:

- a) The offer shall be made by notice specifying
 - i) the number of shares offered and
 - ii) limiting a time not being less than 15 days and not exceeding 30 days from the date of the offer within which the offer, if not accepted, shall be deemed to have been declined;
- b) unless the AOA of the company otherwise provide, the offer aforesaid shall be deemed to include a right to renounce the shares offered to him or any of them in favour of any other person; and the notice shall contain a statement of this right.
- c) After the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the BOD may dispose of them in such manner which is not dis-advantageous to the shareholders and the company.

CONCLUSION: In the above case the allotment would be valid unless it is proved that the shares were allotted to Directors on terms unfavourable to the Company.

Q.No.2. Apex Metals Limited wants to provide financial assistance to its employees, to enable them to subscribe for certain number of fully paid shares. Considering the provision of the Companies Act, 2013, what advice would you give to the company in this regard? **(OLD PM, MTP M17, RTP N18(N))**

PROVISIONS OF LAW: U/s 67(2) of the Companies Act, 2013 no public company is allowed to give, directly or indirectly or by means of a loan, guarantee, or security, any financial assistance for the purpose of, or in connection with, a purchase or subscription, by any person of any shares in it or in its holding company.

However, sec 67(3) makes an exception by allowing companies to the give loans to their employees other than its directors or KMP, for an amount not exceeding their 6 months salary with a view to enabling them to purchase or subscribe for fully paid-up shares in the company or its holding company to be held by them by way of beneficial ownership.

Provided that disclosures in respect of voting rights not exercised directly by the employees in respect of shares to which the scheme relates shall be made in the Board's report in such manner as may be prescribed.

Hence, Apex Metals Ltd can provide financial assistance up to the specified limit to its employees to enable them to subscribe for the shares in the company provided the shares are purchased by the employees to be held for beneficial ownership by them. However, the KMP will not be eligible for such assistance.

Q.No.3. The BOD of XYZ Private Limited, a subsidiary of SRN Limited, decides to grant a loan of Rs 2.00 lac to P, the Finance Manager of the company getting salary of Rs.30,000 per month, to buy 400 partly paid-up equity shares of Rs.1,000 each of XYZ Limited. Examine the validity of Board's decision with reference to the provisions of the Companies Act, 2013.

PROVISIONS OF LAW: U/s 67 (3) of the Companies Act, 2013 a company is allowed to give a loan to its employees subject to the following limitations:

- a) The employee must not be a KMP;
- b) The amount of such loan shall not exceed an amount equal to 6 months salary of the employee.
- c) The shares to be subscribed must be fully paid shares

Sec 2(51) defines the "Key Managerial Personnel" (KMP) whereby a KMP includes the chief executive, company secretary, whole time director, Chief Financial Officer or any other officer who may be prescribed.

ANALYSIS AND CONCLUSION: We can assume the Mr. P being a finance manager is not a KMP of the company. Keeping the above provisions of law in mind, the Board's decision is invalid due to 2 reasons:

- a) The amount being more than 6 months salary of Mr P, which should have restricted the loan to Rs 1.8 Lakhs.
- b) The shares subscribed are partly paid shares whereas the benefit is available only for subscribing in fully paid shares.

Q.No.4. MNO Private Limited, a subsidiary of PQR Limited, decides to give a loan of Rs. 4,00,000 to the HR (Human Resource) Manager, who is not a KMP of MNO Private Limited, drawing salary of Rs. 30,000 per month, to buy 500 partly paid-up Equity Shares of Rs. 1000 each in MNO Private Limited. Examine the validity of company's decision under the provisions of the Companies Act, 2013. **(OLD PM, N15 - 5M)**

PROVISIONS: Restrictions on purchase by company or giving of loans by it for purchase of its share:

As per section 67 (3) of the Companies Act, 2013 a company is allowed to give a loan to its employees subject to the following limitations:

- a) The employee must not be a Key Managerial Personnel;
- b) The amount of such loan shall not exceed an amount equal to six months' salary of the employee.
- c) The shares to be subscribed must be fully paid shares

Section 2 (51) of the Companies Act, 2013 defines the "Key Managerial Personnel" (KMP) whereby a KMP includes the Chief Executive, Company Secretary, Whole Time Director, Chief Financial Officer or any other officer who may be prescribed.

ANALYSIS: In the given instance, HR Manager is not a KMP of the MNO Private Ltd. He is drawing salary of Rs. 30, 000 per month and loan taken to buy 500 partly paid up equity shares of Rs.1000 each in MNO Private Ltd.

CONCLUSION: Keeping the above provisions of law in mind, the company's (MNO Private Ltd.) Decision is invalid due to two reasons:

- a) The amount of loan being more than 6 months' salary of the HR Manager, which should have restricted the loan to Rs. 1.8 Lakhs.
- b) The shares subscribed are partly paid shares whereas the benefit is available only for subscribing fully paid shares.

SECTION 5: SECTION NUMBERS

CONCEPT	SECTION NO.
Alteration of share capital	61
Right shares or right of preemption (Further issue of shares)	62
Issue of bonus shares	63
Notice to be given to registrar for alternation of share capital etc.	64
Reduction of share capital	66
Purchase by company of its own shares	67
Buy-back of securities	68
Transfer of certain sums to CRR A/c	69
Prohibition of buy-back in certain circumstances	70

PENALTY

SECTION	PARTICULARS	PENALTY
Section 61	Punishment in improper issue or conversion of shares into stock	Company and every officer of the company who is in default a. Fine which may extend to Rs.1,000 for each day of default or b. Rs.5 lakhs, whichever is less.
Section 64- Notice to be given to Registrar for alteration of share capital	If a Company fails to file notice to Registrar after alteration of Share Capital.	Company, Officer in Default Company Fine which may extend to Rs 1,000 / day during which such default continues, or Rs 5 Lac whichever is less.
Section 67- Restrictions on Purchase by Company or Giving of Loans by it for Purchase of its Shares	Contravention of the provisions of sec 67	Company, Officer in Default Company : Rs 1 Lac to 25 Lac Officer in Default Company: Fine: Rs 1 Lac to 25 Lac Imprisonment: May extend to 3 years
Section 68- Power of company to purchase its own securities	If a Company does not follow the provisions of buy back of Securities as provided in Sec 68 or any regulation made by SEBI	Company, Officer in Default Company: Rs 1 Lac to 3 Lac Officer in Default Company: Fine: Rs 1 Lac to 3 Lac Imprisonment: May extend to 3 years Or both
Section 447- Punishment for Fraud	Section 447- Punishment for Fraud	Any person who is found to be guilty of fraud i). Involving an amount of at least Rs 10 Lac or 1% of the turnover of the company, whichever is lower Fine: At least amount involved in the fraud, which may extend to 3 times the amount involved in the fraud, and Imprisonment: 6 months to 10 years Also, if fraud in question involves public interest, the term of imprisonment shall not be less than 3 years. ii). Where fraud involves an amount less than Rs 10 Lac or 1% of the turnover of the company, whichever is lower, and does not involve public interest, Fine: May extend to Rs 50 Lac Imprisonment: May extend to 5 years, or both

TIME - LIMITS

PARTICULARS	TIME-LIMIT
Time limit for having right to vote on all resolutions placed before the company for preference shareholders.	Dividend in respect of a class of preference shares has not been paid for a period of 2 years or more.
Notice to ROC for alteration of share capital along with an altered MOA (sec 64) or Diminution of share capital. or redemption of preference shares	within a period of <u>30 days</u> of such alteration.
Time limit for opening of notice for offering of further issue of shares	Not less than 15 days and not exceeding 30 days from the date of the offer.
Time limit for dispatch of notice for offering of further issue of shares	Atleast 3 days before the opening of the issue.
Time limit for making an appeal to tribunal, in case the terms and conditions of such conversion are not acceptable to the company	Within 60 days from the date of communication of such non acceptance by the company.
Time limit conditions for buy-back of shares (Sec 68)	<ul style="list-style-type: none"> • Minimum time gap of 1 year from the date of the closure of the preceding offer of buy-back. • Every buy-back shall be completed within 12 months from the date of passing of SR or BR for authorising the buy-back. • Affidavit shall declare that it will not rendered insolvent within 1 year of date of D.O.S. • Prohibition on further issue of similar securities for a period of 6 months with certain exceptions. • Return of Buy-back has to be filed with the ROC and SEBI within 30 days with necessary details.

THE END

Copyrights Reserved To **MASTER MINDS COMMERCE INSTITUTE PVT.LTD.**